



Southwestern Bell Corporation

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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May 11, 1994

Karol M. Sweltzer
Director
Federal Regulatory

Ex Parte

Mr. William F. Caton, Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: CC Docket No. 93-251 and 93-215

In accordance with Commission rules governing ex parte presentations, please be advised that today, May 11th, Ms. Kathleen Larkin, District Manager-State Regulatory Issues (Southwestern Bell Telephone), Tom Powers, Area Manager-Affiliate Services (Southwestern Bell Telephone), and the undersigned met with Mr. Bill Kehoe, Mr. Ken Ackerman and Mr. Ed Dashkin, all from the Accounting and Audits Division of the Common Carrier Bureau, regarding the proceeding listed above. Attached is a handout provided in the meeting.

If you have any questions, please let me know.

Sincerely,

Attachment

cc: Mr. Bill Kehoe
Mr. Ken Ackerman
Mr. Ed Dashkin

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SOUTHWESTERN BELL TELEPHONE COMPANY
AFFILIATE TRANSACTIONS
CC DOCKET 93-251

I. THE PRIMARY AREAS OF CONCERN AND OPPOSITION TO THE NPRM ARE ROOTED IN THE HISTORY OF THE JOINT COST ORDER (86-111)

A. Estimated Fair Market Valuation for services would:

1. Eliminate economies of scope and scale
(86% of SWBT affiliate transactions are with Bellcore, SBC and Yellow Pages affiliates)

2. Be subjective, difficult to audit and costly

B. Prevailing Price Bright Line Test would be inconsistent with the goals of the Joint Cost Order that
" . . . regulated markets to produce results as close as possible to the results of unregulated markets. . ."

II. THE ADOPTION OF ESTIMATED FAIR MARKET VALUE (EFMV) AS A VALUATION METHOD WEAKENS RATHER THAN ENHANCES AFFILIATE TRANSACTION RULES

A. Provides no added safeguards against cross subsidy - which is the real threshold issue

B. EFMV was previously rejected because it is fraught with the **potential for abuse** and difficulty in monitoring

C. EFMV at best produces a range of market prices. That range is subject to **continuous disagreement** on comparability

D. EFMV results in **complexity and subjectivity** in the **audit process** - results in increased **cost and subjectivity** in the application of the rules

E. EFMV cannot be applied to all services - providers do not exist

F. Cost to establish a valid study is staggering - **SWBT** estimates **\$5.9M/USTA** industry estimate **\$90M+** and the cost of EFMV study exceeds revenue derived from many services

H. Current rule (third tier of fully distributed cost) is cost based and is based on seven years of experience

- I. The Commission has constantly reinforced its position that **Fully Distributed Cost** is a strong safeguard against cross-subsidy, and allows ratepayers to participate in the **economies of scope and scale** as well as assuring a **contribution to common costs**

III. **75% BRIGHT-LINE TEST DENIES THE LEGITIMACY OF A PREVAILING PRICE AND REDUCES THE SPECIFICITY OF THE CURRENT PREVAILING PRICE RULE**

- A. Replaces a specific item by item review with an arbitrary percentage test
- B. If a tariff rate is the first tier of a test (noting that a tariff is a surrogate for a market rate) then a **prevailing price** (a price actually paid by third parties in the market place) on an **item by item basis** should be more acceptable than tariff
- C. A **prevailing price** is established when **"a seller is ready and willing to sell and a buyer is ready and willing to buy in the ordinary course of trade."** An arbitrary percentage does not constrain that transaction.
- D. There is nothing unique about affiliates rendering goods and products at prevailing price - it is a fair measure of true market value.

IV. **THE NPRM PROPOSALS EFFECTIVELY LIMIT THE USE OF PREVAILING PRICE AND REPLACE IT WITH A NEW TIER OF SUBJECTIVE AND UNDEFINED ESTIMATED FAIR MARKET VALUATION - A DUAL BASIS TEST FOR SERVICES ADDS A LAYER OF COST AND ADMINISTRATION WITHOUT RESULTANT BENEFIT**

V. **ADMINISTRATION GOALS AND OTHER ISSUES BEFORE THIS COMMISSION POINT TOWARD SIMPLIFICATION**

VI. **OTHER ISSUES**

- A. **CHAINING** - Already addressed in the existing rules - perceived "harm" is unfounded
1. Current rules reinforce the carrier's natural incentive to derive lowest price for purchases
 2. The proposed "tracing" methods result in **insurmountable cost**, without resultant benefit

- B. The Commission should not regulate the price of transactions between a carrier's nonregulated operations and its nonregulated affiliate
- C. The proposals for estimating, monitoring the estimates and the true up process are not appropriate - If an estimate is used and a true-up is required, SWBT's experience is this is a nominal amount and can be reflected within the next accounting period